

ADJUSTMENT TO BASIS RULE.

The adjustment to basis rule for purposes of depreciation is designed to favor certified historic rehabilitation projects. In this 25 percent category, half of the credit can be included in the depreciable basis. In the 15 and 20 percent categories, however, none of the credit can be depreciated.

EXAMPLE: In a certified historic rehabilitation project where \$100,000 in rehabilitation expenses were incurred, the owner takes a \$25,000 credit on federal income taxes owed. The owner is then allowed to include \$87,000 (\$100,000 - \$12,500) in the depreciable basis. In a non-historic rehabilitation of a 40-year old building where \$100,000 in rehabilitation expenses were incurred, the owner takes a \$20,000 credit on federal income taxes owed, and can then include \$80,000 (\$100,000 - \$20,000) in the depreciable basis.

Depreciation must be calculated straight line and the cost recovery period for all buildings placed in service after March 16, 1984 is 18 years. The property owner may, however, elect to use an accelerated cost recovery on the shell of the building rather than straight line.

THE WALL TEST

ERTA '81 required that 75 percent of the existing external walls must remain in place as external walls in order to qualify as a certified rehabilitation. The Tax Reform Act of 1984 gives developers an alternative test, effective January 1, 1984. If a project fails the ERTA '81 wall test, the following test may now apply: 1) 50 percent of the existing external walls must remain in place as external walls, 2) 75 percent of the existing external walls must remain in place as internal or external walls, and 3) 75 percent of the internal structural framework must remain in place during the rehabilitation process.

RECAPTURE RULES

The owner of a qualified rehabilitated property may be faced with recapture of a portion of the ITC if the property is sold within five years of completion. The recapture is calculated at a rate of 20 percent per year. After five years there is no recapture.

LEASES

A lessee of a qualified rehabilitated property is eligible for the ITC if, on the date that the rehabilitation is completed, the remaining term of the lease is 15 years or more. The qualified rehabilitation may be undertaken by either the lessor or lessee.

A lessee of a portion of a rehabilitated property is also eligible for the ITC if all requirements for obtaining the ITC have been met with respect to the whole building. That is, the rehabilitation of the whole building must be certified as appropriate by the Department of the Interior and must meet the substantial rehabilitation test, using the lessor's adjusted basis. The lessee is then eligible for the pro rata share of the ITC based on the space leased.

In the case of an owner-occupied, multi-family structure which had been rehabilitated using the preservation tax incentives, that portion of the building which is income-producing is eligible for the tax credit.

EASEMENTS

Owners of historic properties may elect to contribute easements to a unit of government or a publicly supported charity. The easement assures the perpetual preservation of a site or a feature of a historic property, such as a facade. By so doing, the property owner reduces the value of the property because future development of the site or adverse changes to the structure are not allowed after the easement is donated.

In some cases, an easement donation is used in conjunction with the ITC. Since the donation reduces the value of the property, the adjusted basis is also reduced and the substantial rehabilitation test is met by lower rehabilitation expenditures.

Easement donations may be associated with depreciable or non-depreciable historic properties. Part 1 of the certification application is used in the easement donation process.

TAX-EXEMPT USE

Any property in a tax-exempt use will be denied the ITC for expenses incurred in the rehabilitation of that portion of the building occupied in tax-exempt use. In addition, that same portion of the building must be depreciated over 40 years, rather than 18, or 125 percent of the lease term, whichever is greater.

Tax-exempt use is defined as: 1) A property that is financed by tax-exempt bonds and the tax-exempt organization participated in such financing; 2) A property leased with a fixed price purchase option; 3) Property leased for a term greater than 20 years; 4) Property in a sale-leaseback or lease leaseback situation; and 5) A property where more than 35 percent of the net rentable floor area is used by a tax-exempt organization.

APPEALS

Any decision made by the Department of the Interior regarding certifications may be appealed. The appeal must be in writing and received by the Chief Appeals Officer at the Department of the Interior within 30 days of receipt of the decision which is being appealed. The property owner may request a meeting with the appeals officer or send a representative. In most cases, the property owner may expect a decision on the appeal within 30 days of receipt by the Department of the Interior.